

the intended date of settlement is one to two days after the recording of the transaction by MCC.

MCC has requested that the proposed rule change become effective on the same date as Rule 15c6-1. Rule 15c6-1 becomes effective on June 7, 1995.<sup>5</sup>

## II. Discussion

The Commission believes the proposal is consistent with the requirements of Section 17A of the Act.<sup>6</sup> Specifically, Section 17A(b)(3)(F)<sup>7</sup> states that the rules of a clearing agency must be designed to assure the safeguarding of securities and funds which are in the MCC's custody or control or for which MCC is responsible and must be designed to foster cooperation and coordination with persons engaged in the clearance and settlement of securities transactions. Several of MCC rules are based on a five day time frame for settlement of securities transactions. On June 7, 1995, the new settlement cycle of T+3 will be established as mandated by the Commission's Rule 15c6-1. As a result, the MCC's current rules will be inconsistent with the Commission's rule. This proposal will amend the MCC's rules to harmonize them with Commission's Rule 15c6-1 and a T+3 settlement cycle.

## III. Conclusion

For the reasons stated above, the Commission finds that MCC's proposal is consistent with Section 17A of the Act.<sup>8</sup>

It is therefore ordered, pursuant to Section 19(b)(2) of the Act,<sup>9</sup> that the proposed rule change (File No. SR-MCC-94-16) be and hereby is approved and will become effective June 7, 1995.

For the Commission by the Division of Market Regulation, pursuant to delegated authority.<sup>10</sup>

**Margaret H. McFarland,**

*Deputy Secretary.*

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<sup>5</sup> The transition from five day settlement to three day settlement will occur over a four day period. Friday, June 2, will be the last trading day with five business day settlement. Monday, June 5, and Tuesday, June 6, will be trading days with four business day settlement. Wednesday, June 7, will be the first trading day with three business day settlement. As a result, trades from June 2 and June 5 will settle on Friday, June 9. Trades from June 6 and June 7 will settle on Monday, June 12.

<sup>6</sup> 15 U.S.C. 78q-1 (1988).

<sup>7</sup> 15 U.S.C. 78q-1(b)(3)(F) (1988).

<sup>8</sup> 15 U.S.C. 78q-1 (1988).

<sup>9</sup> 15 U.S.C. 78s(b)(2) (1988).

<sup>10</sup> 17 CFR 200.30(a)(12) (1994).

[Release No. 34-35507; File No. SR-NASD-94-56]

## Self-Regulatory Organizations; National Association of Securities Dealers, Inc.; Order Granting Partial Approval of Proposed Rule Change Relating to the Three Business Day Settlement of Securities Transactions

March 17, 1995.

On October 12, 1994, the National Association of Securities Dealers, Inc. ("NASD") filed with the Securities and Exchange Commission ("Commission") a proposed rule change pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 ("Act").<sup>1</sup> On November 9, 1994, the NASD filed with the Commission Amendment No. 1.<sup>2</sup> The purpose of the proposed rule change is to amend the NASD's rules to provide for three business day settlement of securities transactions. The Commission published notice of the proposed rule change in the **Federal Register** on November 18, 1994.<sup>3</sup> The commission granted partial, accelerated approval of the proposed rule change on November 30, 1994.<sup>4</sup> On December 8, 1994, the NASD filed with the Commission Amendment No. 2.<sup>5</sup> The amendments were technical amendments that did not require republication of notice. One comment was received on the notice.<sup>6</sup> As discussed below, the Commission is approving that portion of the proposed rule change relating to the three day settlement of securities transactions.<sup>7</sup>

<sup>1</sup> 15 U.S.C. 78s(b)(1) (1988).

<sup>2</sup> Letter from Suzanne E. Rothwell, Associate General Counsel, NASD, to Mark Barracca, Branch Chief, Over-the-Counter Regulation, Division of Market Regulation, Commission (November 8, 1994).

<sup>3</sup> Securities Exchange Act Release No. 34966 (November 10, 1994), 59 FR 59802.

<sup>4</sup> Securities Exchange Act Release No. 35031 (November 30, 1994), 59 FR 62761. The order approved that portion of the proposed rule change relating to the transfer of customer accounts between broker-dealers.

<sup>5</sup> Letter from Suzanne E. Rothwell, Associate General Counsel, NASD, to Mark Barracca, Branch Chief, Over-the-Counter Regulation, Division of Market Regulation, Commission (December 7, 1994). Amendment No. 2 eliminated the proposed amendment to Section 64(a)(3) which would have shortened the time for confirmation of a customer order from the day after trade date to the trade date. Amendment No. 2 also lengthened by one day, from the first day after trade date to the second day after trade date, the time for a buying customer to provide agent instructions under Section 64(a)(4).

<sup>6</sup> Letter from P. Howard Edelstein, President, Electronic Settlements Group, Thomson Trading Services, Inc. (A Thomson Financial Services Company), to Jonathan G. Katz, Secretary, Securities and Exchange Commission (December 2, 1994).

<sup>7</sup> With this order, the Commission has now approved all of File No. SR-NASD-94-56.

## I. Description

On June 7, 1995, the standard settlement time frame for most securities transactions will be shortened from five business days after the trade date ("T+5") to three business days after the trade date ("T+3").<sup>8</sup> The proposal amends certain provisions of the NASD's Uniform Practice Code ("UPC") and the rules of Fair Practice ("RFP") consistent with a T+3 settlement cycle. These amendments will become effective on the same date as Commission Rule 15c6-1, which establishes T+3 as the standard settlement time frame.<sup>9</sup>

The proposed rule change will shorten the time periods established under the NASD's rules for taking certain actions related to settlement. Currently, Section 12(b) of the UPC states that for a regular way transaction delivery must be made on, but not before, the fifth business day following the trade date. The proposal shortens the delivery requirement to on, but not before, the third business day following the trade date. In addition, seller's option transaction deliveries may be made by the seller on any business day after the third business day, rather than after the fifth business day, following the trade date.

Similarly, Article III, Section 26(m)(1) of the RFP is amended to require that members transmit payments received from customers for the purchase of investment company shares within three business days, rather than within five business days, after receipt of such customers' purchase orders or one business day following receipt of customer payments, whichever is later.

Section 64(a)(4) of the UPC currently requires that customers that use an agent to pay for or to deliver securities must agree to furnish instructions to the agent no later than T+4 if buying on a receipt versus payment ("RVP") basis or no later than T+3 if the customer is selling on a delivery versus payment ("DVP") basis. The proposed rule

<sup>8</sup> On October 6, 1993, the Commission adopted Rule 15c6-1 under the Act (17 CFR 240.15c6-1), which establishes T+3 instead of T+5 as the standard settlement time frame for most broker-dealer transactions. Securities Exchange Act Release No. 33023 (October 6, 1993), 58 FR 52891. The rule becomes effective June 7, 1995. Securities Exchange Act Release No. 34952 (November 9, 1994), 59 FR 59137.

<sup>9</sup> The transition from five day settlement to three day settlement will occur over a four day period. Friday, June 2, will be the last trading day with five business day settlement. Monday, June 5, and Tuesday, June 6, will be trading days with four business day settlement. Wednesday, June 7, will be the first trading day with three business day settlement. As a result, trades from June 2 and June 5 will settle on Friday, June 9. Trades from June 6 and June 7 will settle on Monday, June 12.

change shortens the time period for furnishing such instructions to T+2 and T+1 for buying and selling customers, respectively.<sup>10</sup>

The Prompt Receipt and Delivery Interpretation of the Board of Governors, Article III, Section 1 of the RFP requires each member to make an affirmative determination that its customer owns the security and will deliver it in good deliverable form within five business days of the execution of an order in connection with a long sale. The interpretation also states that to satisfy the requests for an affirmative determination, the member must note on the order ticket at the time of the order the customer's ability to deliver the securities within five business days. The proposed rule change changes these time limits from five business days to three business days.

To accommodate a three business day settlement cycle, it will be necessary to change the ex-dates with respect to cash and stock dividends, warrants, and interest.<sup>11</sup> Section 5(b)(1) of the UPC currently provides that the ex-date with respect to cash dividends or distributions, stock dividends, or warrants which are less than 25% of the value of the security shall be the fourth business day preceding the record date of the fifth business day preceding the record date if the record date falls on a day designated as a non-delivery date provided that definitive information is received sufficiently in advance of the record date. Section 6(a) currently provides that all transactions, other than cash transactions, in bonds or other instruments of indebtedness which are traded flat shall be ex-interest on the fourth business day preceding the record date if the record date falls on a business day, on the fifth business day preceding the record date if the record date does not fall on a business day, and on the fifth business day preceding the date on which an interest payment is to be made if no record date has been fixed. All of the time frames contained in Sections 5(b)(1) and 6(a) are being shortened by two business days. All the other time frames contained in Sections 5 and 6 of the UPC are not being changed.

<sup>10</sup> Section 64(a)(3) of the UPC currently requires that members accepting an order whereby payment or delivery is to be made to or by an agent of the customer must deliver a confirmation no later than T+1. The notice of the proposed rule change indicated that this time period would be shortened to trade date. The NASD has withdrawn this portion of the rule change. *Supra* note 5.

<sup>11</sup> The ex-date indicates the interval between the announcement and payment of a distribution during which time an investor who purchases shares is not entitled to the distribution.

Section 46 of the UPC currently requires that interest to be added to the price of interest-paying securities be calculated up to but not including the fifth business day following the date of the transaction. The proposed rule change shortens the time frame so that interest is calculated up to but not including the third business day.

## II. Comments

The Commission received one comment letter from Thomson Trading Services, Inc. ("Thomson") suggesting that additional regulatory changes may be necessary to implement T+3 settlement.<sup>12</sup> Thomson believes that the NASD should amend Section 64 of the UPC which requires the use of a registered clearing agency's facilities for automated confirmations and acknowledgements.

## III. Discussion

The Commission believes the proposed rule change is consistent with Section 15A of the Act and, therefore, is approving the proposal. Specifically, the Commission believes the proposal is consistent with Section 15A(b)(6)<sup>13</sup> of the Act which requires that the rules of the NASD be designed to foster cooperation and coordination with persons engaged in regulating, clearing, settling, processing information with respect to, and facilitating transactions in securities, to remove impediments to and perfect the mechanism of a free and open market and a national market system, and, in general, to protect investors and the public interest.

Currently, the rules of the NASD and other self-regulatory organizations control the time frame for settlement of securities transactions. On June 7, 1995, the new settlement cycle of T+3 will be established as mandated by the Commission's Rule 15c6-1.

As a result, the NASD's current rules for a T+5 settlement cycle will be inconsistent with the Commission's rule. This proposal amends the NASD's rules to harmonize them with the Commission's Rule 15c6-1 and a T+3 settlement cycle.

The commission believes that the benefits of a three day settlement cycle, as outlined in the release adopting Rule 15c6-1, apply equally to the NASD's proposed rule change.<sup>14</sup> With a T+3 settlement cycle, fewer unsettled trades will be subject to credit and market risk, and there will be less time between trade execution and settlement for the

value of those trades to deteriorate.<sup>15</sup> By reducing risk to the clearance and settlement system, the NASD's proposed rule change furthers Section 15A's goals of protection of investors and of the public interest. The NASD's rules will assist the transition to a T+3 cycle by providing guidelines for related matters such as ex-dates and delivery of agent instructions. Thus, the proposed rule change is consistent with Section 15A's goals of fostering cooperation and coordination with persons engaged in regulating, clearing, and settling transactions in securities and of perfecting the mechanism of a free and open market.

While Thomson's letter supports the NASD's efforts to shorten the settlement cycle for securities transactions, Thomson believes that the NASD should amend Section 64 of the UPC, which requires the use of a registered clearing agency's facilities for automated confirmation and acknowledgement of all DVP/RVP transactions.<sup>16</sup> The NASD, in response to Thomson's letter, states that the NASD opposes amending Section 64 because Thomson's system is not interfaced with other providers of confirmation/acknowledgement services and because Thomson is not subject to regulatory oversight.<sup>17</sup> The NASD also states that Thomson's letter raises significant issues as to whether a third-party vendor of confirmation/affirmation services should be recognized to be equivalent to a registered clearing organization providing such services.<sup>18</sup> Thomson provided a further comment letter

<sup>15</sup> The Commission's release adopting Rule 15c6-1 stated that "the value of securities positions can change suddenly causing a market participant to default on unsettled positions. Because the markets are interwoven through common members, default at one clearing corporation or by a major market participant or end-user could trigger additional failures, resulting in risk to the national clearance and settlement system." *Id.*

<sup>16</sup> Thomson asserts that Section 64 precludes vendors such as Thomson from competing with The Depository Trust Company ("DTC"), a registered clearing agency. Letter from Thomson, *supra* note 6. The self-regulatory organization confirmation trades to the facilities of a registered securities depository. These rules, however, were designed to facilitate high levels of trading volume. Further, as in the T+5 settlement cycle, an institutional investor will be free to choose the post-trade communication service provider as long as the trade is eventually confirmed and acknowledgement through a registered securities depository.

<sup>17</sup> Letter from Elliott R. Curzon, Assistant General Counsel, NASD, to Christine Sibille, Senior Counsel, Office of Securities Processing, Division of Market Regulation, Commission (December 21, 1994).

<sup>18</sup> Letter from Suzanne E. Rothwell, Associate General Counsel, NASD, to Christine Sibille, Senior Counsel, Office of Securities Processing, Division of Market Regulation Commission (January 26, 1995).

<sup>12</sup> Letter from Thomson, *supra* note 6.

<sup>13</sup> 15 U.S.C. § 78o-3(b)(6) (1988).

<sup>14</sup> *Supra* note 7.

asserting that provision of a trade confirmation was not a depository function and therefore did not require the use of a depository registered with the Commission.<sup>19</sup>

The Commission believes that the issues raised by the Thomson letter need not be resolved prior to the approval of the NASD's proposed rule change. Discussions regarding Thomson's concern are underway among the Commission, Thomson, and DTC. DTC has submitted a rule filing that will establish a linkage between DTC and vendors such as Thomson.<sup>20</sup> The Commission intends to consider whether self-regulatory organization rules should continue to preclude use of private vendor systems for confirmation/affirmation services in DVP/RVP trades. However, if the NASD's proposed rule change being approved by this order is not approved prior to the June 7, 1995, effective date of the Commission's Rule 15c6-1, the NASD rules will conflict with the Commission Rule 15c6-1.

As discussed above, Thomson's letter suggests that approval of the proposed rule change without amendments to Section 64 raises competitive concerns. Under the Act, the Commission's responsibility is to balance the perceived anticompetitive effects of a regulatory policy or decision against the purpose of the Act that would be advanced by the policy or decisions and the costs associated therewith. The Commission notes that any anticompetitive effects pointed to by Thomson are not caused by the proposed rule change being approved by this order but rather by an existing NASD rule. The Commission is reviewing Thomson's claim but does not believe that approval of this proposal will itself create any burdens on competition. Moreover, as discussed above, the rule advances fundamental purposes under the Act, namely the efficient clearance and settlement of securities.

#### IV. Conclusion

For the reasons stated above, the Commission finds that the portion of the proposed rule change relating to three day settlement of securities transactions is consistent with Section 15A of the Act.

It is therefore ordered, pursuant to Section 19(b)(2) of the Act, that the

portion of the rule change (File No. SR-NASD-94-56) containing the amendments to Sections 5, 6, 12, 46, and 64 of the UPC and Article III, Section 26(m)(1) and Article III, Section 1 of the RFP be and hereby is approved and will become effective on June 7, 1995.

For the Commission by the Division of Market Regulation, pursuant to delegated authority.<sup>21</sup>

**Margaret H. McFarland,**

*Deputy Secretary.*

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[Release No. 34-35506; File No. SR-NYSE-94-40]

#### Self-Regulatory Organizations; New York Stock Exchange, Inc.; Order Approving Proposed Rule Change Relating to Implementation of a Three-Day Settlement Standard

March 17, 1995.

On November 3, 1994, the New York Stock Exchange, Inc., ("NYSE") filed a proposed rule change (File No. SR-NYSE-94-40) with the Securities and Exchange Commission ("Commission") pursuant to Section 19(b) of the Securities Exchange Act of 1934 ("Act").<sup>1</sup> Notice of the proposal was published in the **Federal Register** on December 23, 1994 to solicit comments from interested persons.<sup>2</sup> The Commission received one comment letter.<sup>3</sup> As discussed below, this order approves the proposed rule change.

#### I. Description

In October 1993, the Commission adopted Rule 15c6-1 under the Act<sup>4</sup> which establishes three business days after the trade date ("T+3"), instead of five business days ("T+5"), as the standard settlement cycle for most securities transactions. The rule will become effective June 7, 1995.<sup>5</sup> Several of the current NYSE's rules are interrelated with a T+5 settlement time frame. The purpose of the rule change is to amend NYSE's rules to be

consistent with a T+3 settlement standard for securities transactions.

NYSE Rules 64(a)(3), 65(b), and 85(d)(3) specify the delivery date for securities sold in regular way transactions, odd lot sales, and cabinet sales, respectively. The time frames contained in each rule is being shortened to conform to a T+3 settlement cycle. Rule 64(a)(5) currently provides that on the second, third, fourth, and fifth business days preceding the final day for subscription, bids, and offers in rights to subscribe shall be made only for delivery next day. This section is being amended to eliminate references to the fourth and fifth business days. Rule 64(c) is being amended to provide that seller's option trades can settle on the third business day, rather than the fifth business day, after the trade date.

Rule 235 is being amended to provide that transactions in stocks shall be ex-dividend or ex-rights on the second business day preceding the record date rather than on the fourth business day. With regard to a record date on a day other than a business day, transactions in stocks shall be ex-dividend or ex-rights on the third preceding business day rather than on the fifth preceding business day. The time frame contained in Rule 257 for delivery of dividends or rights for securities sold before the "ex" date but delivered after the record date is being shortened to three days after record date.

Rule 236 prescribes when ex-warrant trading will begin. The ex-warrant period is being changed to the second business day preceding the date of expiration of the warrants instead of the fourth business day. When warrant expiration occurs on other than a business day, the ex-warrant period will begin on the third business day preceding the expiration date instead of on the fifth business day.

Rule 387(a)(4) requires a member to obtain an agreement from its customer to deliver instructions to its agent within certain time periods with respect to receipt and delivery of securities sold delivery versus payment ("DVP") or receipt versus payment ("RVP"). All the time frames contained in Rule 387(a)(4) are being shortened by two days. Rule 123A.32 currently states that the liability of a specialist shall not extend beyond the closing price on the third business day where it is deemed that the specialist did not send out a report. This time frame is being shortened by two business days. The proposal shortens the time frames contained in Rule 123B(b)(2) (A) and (B) for correcting

<sup>21</sup> 17 CFR 200.30-3(a)(12) (1994).

<sup>1</sup> 15 U.S.C. 78s(b) (1988).

<sup>2</sup> Securities Exchange Act Release No. 35110 (December 16, 1994), 59 FR 35011.

<sup>3</sup> Letter from Dr. Keith B. Jarrett, President, Thomson Trading Services, Inc., to Jonathan G. Katz, Secretary, Commission (January 12, 1995).

<sup>4</sup> 17 CFR 240.15c6-1.

<sup>5</sup> Securities Exchange Act Release Nos. 33023 (October 6, 1993), 58 FR 52891 (order adopting Rule 15c6-1) and 34952 (November 9, 1994), 59 FR 59137 (order changing the effective date from June 1, 1995, to June 7, 1995).

<sup>19</sup> Letter from P. Howard Edelstein, President, Electronic Settlements Group, Thomson, to Jonathan G. Katz, Secretary, Commission (February 1, 1995).

<sup>20</sup> Securities Exchange Act Release No. 35332 (February 3, 1995) 60 FR 8102 (notice of filing of proposed rule change).